North Dakota Office of State Tax Commissioner

### 1998

# Income tax update

News and developments for tax practitioners

Year-end edition October 1998

#### A publication of the Income and Oil Taxes Division

Rick Clayburgh Tax Commissioner

### It's time to order '98 tax forms

Enclosed with this first edition of *Income* tax update is the order form for the 1998 North Dakota income tax forms.

One change you should note in the items listed on the order form pertains to the ordering of Form 400-ES. If you order Form 400-ES, no envelopes (for submitting payments) will automatically be included with your order. The envelope is now listed separately on the order form and must be ordered separately.

Please order only what you'll think you'll need for the upcoming tax season. An extra order blank will be enclosed with your order in case you need to reorder. Your consideration in this regard helps us to keep printing costs to a minimum.

If you don't receive your order in a reasonable amount of time, please do not submit

a new order. Instead, you may check on your order by calling (701)328-3017. If calling from within North Dakota, use our toll-free number 1-800-638-2901 (but do not select any of the five option—wait for assistance and ask for extension 8-3017). If you are speech or hearing impaired, call us through Relay North Dakota at 1-800-366-6888 (and ask for 1-800-638-2901).

Don't forget that in a pinch, forms and instructions can be downloaded from our Internet web site at www.state.nd.us/taxdpt.

We are striving for good customer service, and we invite your suggestions and comments on how we can better serve your needs. Have a successful tax season!

### In this issue

- 1 Ordering '98 forms Magnetic filing of W-2s and 1099s
- 2 Financial institution tax developments Income tax exemption reporting by pass-thru
- 3 Family member care tax credit FAQS Electronic filing and payment options Effect of new federal tax credits on Form 37-S
- 4 Social security number removed from label Changes to '98 forms Expiration of alternative fuels tax credit

# Magnetic filing of W-2s and 1099s will soon be required

The North Dakota Office of State Tax Commissioner (Tax Department) will soon require the filing of information returns—Form W-2 and Form 1099—on magnetic media by employers and payors. While the Tax Department currently accepts this information in the same magnetic media formats used for federal purposes, a number of employers and payors who file on magnetic media for federal purposes continue to file paper with North Dakota.

Starting with the information returns to be filed for the 1999 calendar year (which are due on February 28, 2000), the Tax Department will require employers and payors to file information returns on magnetic media if they are required to file them on magnetic media for federal purposes. Under federal law, magnetic media reporting is required for 250 or more information returns.

If the new magnetic media filing requirement for 1999 poses a hardship for an employer or payor, a written request for waiver

of the requirement may be submitted to the Tax Department for consideration.

All registered employers will be notified by mail in early 1999 of the new Form W-2 magnetic media filing requirement.

The information returns for the 1998 calendar year (which are due on February 28, 1999) may be filed on magnetic media or paper. However, the Tax Department encourages employers and payors to consider filing them on magnetic media.

Another option for filing Form 1099 is the Fed/State Combined Reporting Program. Under this program a payor who files 1099s with the IRS on magnetic media may authorize the IRS (using Federal Form 6847) to automatically forward a copy of the 1099 information to the Tax Department. The payor must provide advance written notice to the Tax Department if this filing method is elected.

For more information, contact the Magnetic Media Coordinator, Withholding Section. See page 4 for contact information.

# Financial institution tax developments

### Electronic filing is successful for '97!

For 1997, financial institutions were required to complete the new North Dakota financial institution tax return, Form 35, using a computer program developed by the North Dakota Office of State Tax Commissioner (Tax Department). The first year of this new filing method went smoothly, and the Tax Department considers the initiative a success.

The computer program is obtained by either downloading it from the Tax Department's Internet web site or requesting a set of diskettes from the Tax Department. Using a personal computer, the return is prepared electronically and stored to a blank diskette. The diskette with the completed return, a properly completed remittance form, and any required supporting paper documents are then mailed to the Tax Department for processing.

In response to suggestions received from both taxpayers and return preparers, the computer program was modified for 1998 to allow the user to save a completed return to a hard drive or network drive for recordkeeping purposes.

### Error in '97 income tax instructions for individuals and fiduciaries

In 1997, as part of the major revisions to North Dakota tax law covering financial institutions, a new adjustment was created for certain individuals, estates and trusts. The purpose of the adjustment is to remove income or loss derived from a pass-through entity which is subject to the North Dakota financial institution tax.

However, an error was made in describing this new adjustment in the the 1997 instructions to Form 35 (North Dakota financial institution tax return), Forms 37-S and 37 (North Dakota individual income tax returns) and Form 38 (North Dakota fiduciary income tax return).

In the 1997 instructions, the adjustment was described as applying to income or loss derived from a Subchapter S corporation that is subject to the financial institution tax. However, the reference should have been to *all pass-through entities* subject to this tax. A pass-through entity includes a partnership, Subchapter S corporation, and limited liability company treated like a partnership.

We apologize for this error. If this error affected your preparation of any 1997 North Dakota income tax return, an amended return may be filed.

#### Pass-through entity reporting of the N.D.C.C. ch. 57-35.3 adjustment amount

If a partnership, Subchapter S corporation, or a limited liability company (treated like a partnership) is subject to the North Dakota financial institution tax (under N.D.C.C. ch. 57-35.3), it must prepare and give a statement to each individual, estate and trust owner explaining the special adjustment that must be made on the owner's North Dakota income tax return.

As an alternative to preparing a separate statement, the entity may report the same information in the Supplemental Information section of the federal Schedule K-1 that it prepares for each applicable owner. It is important that the information be clearly identified as North Dakota tax information, and that the information is important to the preparation of the owner's North Dakota income tax return.

For more information, obtain the Income Tax Guideline: Adjustment For Income (Loss) From S Corporation, Partnership or LLC Subject To N.D.C.C. ch. 57-35.3.

# Income tax exemption reporting by pass-thru entities

If a partnership, Subchapter S corporation, or a limited liability company (treated like a partnership) is granted an income tax exemption under N.D.C.C. ch. 40-57.1 (Tax Exemptions For New And Expanding Businesses), it must not make an adjustment for the exemption when determining its North Dakota income (loss) on Form 58 or Form 60. Instead, the exemption must be passed through to its owners who may subtract their respective shares of the exempt income when calculating their North Dakota taxable incomes.

Please note, however, that if the owner is an individual, estate or trust, no adjustment is allowed if the short-form method (on Form 37-S or Form 38) is used to calculate the North Dakota income tax liability. An individual, estate or trust is allowed to subtract its share of the exempt income only if the long-form method (on Form 37 or Form 38) is used to calculate the North Dakota income tax liability. These owners should compare both methods to see which one benefits them the most.

For more information about the income tax exemption, see N.D.C.C. ch. 40-57.1 and N.D. Admin. Code § 81-03-01.1-06.

**Income tax update** is a publication of the Income and Oil Taxes Division, North Dakota Office of State Tax Commissioner, State Capitol, 600 East Boulevard Avenue, Bismarck, ND 58505-0599.

It is published annually in October and after each legislative session in June. It is intended for tax professionals and other persons interested in developments, updates and other information about North Dakota's income and financial institution tax laws, rules and administrative policies. It is mailed free-of-charge to all persons on the Division's practitioners' mailing list. To get on the list, call (701)328-3450 or (toll free within North Dakota) 1-800-638-2901, or write to the above address. A request may also be sent through our Internet web site at www.state.nd.us/taxdpt.

## Family member care tax credit FAQs

The family member care tax credit was created in 1997 to help certain taxpayers who incur costs for the care of family members to prevent their placement in a long-term care facility. Following are some common questions asked by taxpayers and our answers to them.

### "Can a spouse be a qualifying family member?"

Yes, provided the spouse is at least 65 years old or disabled as determined by the Social Security Administration. In addition, the combined federal taxable income of both spouses must be no more than \$30,000.

# "Can I claim the credit for qualified expenses I incur for my own care?"

No. The taxpayer and the qualifying family member must be different individuals.

#### "Does the Social Security Administration have to make a determination of disability?"

Yes. The law requires that a determination be made by the Social Security Administration. It isn't enough to just meet SSA's disability criteria. A taxpayer who claims the credit on this basis must attach proof of this determination to the tax return.

# "Can I claim the credit for the expense of driving my mother to the doctor?"

No. Although all of the other criteria are met, an expense does not qualify unless the goods or services are provided by an organization or individual not related to either the taxpayer or the qualifying family member.

If you have other questions about the family member care credit, do not hesitate to contact the Office of State Tax Commissioner.

Project 2001 update

# Electronic filing and payment options will be available soon

Two electronic filing and payment options affecting income taxes are off the ground and in the implementation process. They are among the Project 2001 goals set by the North Dakota Office of State Tax Commissioner (Tax Department). Following are brief descriptions of the two projects.

# Telefiling/EFT for income tax withholding

With a touch-tone phone and a few minutes, employers will be able to file their income tax withholding returns and remit the withheld taxes to the state—all at no charge to them.

Using a special toll-free telephone number, an employer may call into the telefile/EFT system where an interactive voice response (IVR) system will guide the employer step-by-step through the entire filing and payment process. Once the return information is verified, an amount equal to the taxes due for the period will be withdrawn from the employer's bank account (through an ACH debit transaction) on the day authorized by the employer.

An employer must register with the Tax Department to use this system. For security purposes, a personal identification number (PIN) chosen by the employer will be assigned when the system is first accessed.

## Fed/State electronic filing for individual income tax

The Tax Department is currently working on the computer program changes that will allow its participation in the IRS's Fed/State Electronic Filing Program. Through this program taxpayers will be able to electronically file their North Dakota individual income tax returns in the same transmission in which they electronically file their federal returns. The IRS will forward the state tax information to the Tax Department for processing.

Initially, Form 37-S (Short form) and, if applicable, Schedule NR will be accepted electronically. In addition, only returns claiming a refund or having no tax due will be accepted. (Returns with payments will not be accepted electronically.)

## When will these options be available?

We are working on having the Fed/State electronic filing option ready for the filing of the 1998 returns. The withholding telefile/EFT option is currently undergoing testing and is expected to be ready in early 1999. Watch for public announcements and mailings for further developments and official startup dates.

## The new federal income tax credits for individuals will not affect the Form 37-S (Short Form) tax calculation

There have been questions on whether the new federal income tax credits—i.e., the child, HOPE scholarship and lifetime learning credits—created by the Taxpayer Relief Act of 1997 (P.L. 105-34, Aug. 5, 1997) will affect the North Dakota individual income tax calculation on Form 37-S (Short Form).

The new federal credits will not affect the calculation of the tax on Form 37-S. Unless specifically provided for in the short-form statute, the federal income tax liability for purposes of Form 37-S is the amount *before* all federal income tax credits except the credit for prior year minimum tax. Note: For Form 37 (Long Form) purposes, the new credits will reduce the amount allowed as a federal income tax deduction in determining North Dakota taxable income.

# Social security number is no longer on address label

In response to taxpayers' requests, the social security number will no longer be printed on the peel-off address label that is attached to the individual income tax booklets and postcards. This will help protect taxpayers' privacy and security.

### Important return preparation reminder!

The removal of the social security number from the peel-off address label makes it very important to print or type the social security number in the box provided on the return. If preparing the return for a married person, also enter the spouse's social security number. Your attention to this preparation detail is appreciated.

# Tax form changes to note for 1998

The 1998 income tax forms remain largely unchanged from last year. A couple of minor technical changes have been made to the individual income tax instructions. In addition, you'll see some changes in the look of the forms and instructions that we believe will improve their readability and instruction. Following are a number of the changes to note for 1998.

### Automatic 2-month extension when outside the U.S.

North Dakota generally recognizes federal extensions to file. This includes the automatic 2-month extension allowed to U.S. citizens or residents who live and work outside the U.S. or Puerto Rico, or who are in military or naval service on duty outside the U.S. or Puerto Rico, on the due date of their federal return.

The instructions to the individual return have been revised to explain what must be done to qualify for this extension for North Dakota purposes. To qualify, a copy of the same statement that the IRS requires to be

attached to the federal return in this situation must be attached to the North Dakota return, and the extension box at the top of the North Dakota return must be checked.

#### Schedule FC instructions

The instructions to Schedule FC (family member care credit) have been revised to provide that if costs are incurred for services, the person or organization providing the services must be identified in a statement attached to the schedule.

### Social security number area of individual returns

Because the social security numbers are no longer printed on the address labels, they must now be printed or typed in the boxes provided on the returns. These boxes have been highlighted on the returns as a reminder to do this.

### Percentage (%) calculation replaced with decimal calculation

Based on questions and comments from taxpayers as well as errors on returns, the percentage calculation using the percentage symbol (%) has been replaced with a decimal calculation throughout the individual and fiduciary forms and instructions.

#### Form 37-S (Short Form) changes

On Form 37-S, the credit for income tax paid to another state (Schedule 4) and the family member care credit (Schedule FC) have been combined into one line (line 11). This change reduces the number of lines on the return from 27 to 25.

### Alternative fuels credit expired

The income tax credit allowed to an individual (on Form 37) or a corporation (on Form 40) for purchasing conversion equipment that allows a motor vehicle to run on alternative fuels, such as natural gas, is no longer available. Pursuant to the expiration clause in the statute, the credit expired on December 31, 1997.

# Your questions and comments are welcome

Your day-to-day, hands-on experience in the accounting and tax environments, and your dealings with North Dakota's taxpayers, make you a valuable resource.

Your input helps us to provide the best service possible, and we invite you to contact us at any time.

#### Thank you.

#### Where to reach us...

#### Phone numbers

Individual income tax
Income tax withholding
Corporation income tax
Sales and special taxes\*

(701)328–3450
(701)328–3125
(701)328–2046
(701)328–3470

(\*Includes sales, use, motor fuels, estate, city lodging, highway contract privilege, and music or dramatico—musical composition performing rights taxes.)

Oil and gas taxes (701)328–2014
Property tax (701)328–3127
Commissioner's office (701)328–2770

Toll free (in North Dakota) 1-800-638-2901

Speech/hearing impaired—Call

Relay North Dakota 1-800-366-6888 (ask for 1-800-638-2901)

Internet web site www.state.nd.us/taxdpt

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#### Comments?

If you have suggestions for articles, or would like to comment on this publication, you may direct them to:

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